

Message Text

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C O N F I D E N T I A L SECTION 01 OF 03 LONDON 01135

LIMDIS GREENBACK

DEPARTMENT PASS TREASURY AND FRB

E.O. 11:652: XGDS-1

TAGS: EFIN, UK

SUBJECT: U.K. VIEWS ON INTERNATIONAL MONETARY REFORM AND
FLOATING FRENCH FRANC

REF: LONDON 1062

SUMMARY: U.K. TREASURY AND BANK OF ENGLAND OFFICIALS WHO
ATTENDED LAST WEEK'S C-20 AND WP-3 MEETINGS, AND THIS
WEEK'S EC MONETARY COMMITTEE MEETING CONSIDER THAT, ON
BALANCE, FRANC FLOAT IS A COMPETITIVE DEVALUATION, BUT
THEY DON'T APPEAR UNDULY WORRIED ABOUT IT; FLOATING OF
FRENCH FRANC SEEN AS ONE MORE DISASTER FOR EUROPEAN
MONETARY UNION. U.K. IS IN GENERAL PLEASED WITH OUTCOME
OF C-20 MEETING ON SDR VALUATION, REVISED IMF STRUCTURE,
AND WITTEVEENS PROPOSAL FOR AN IMF FACILITY, BUT IT
FORESEES DIFFICULTIES IN HAMMERING OUT THE MECHANICS THAT
WOULD BRING THESE AGREEMENTS INTO EFFECT. COMING WEEKS
WILL SEE INTENSE PRESSURE AMONG EC COUNTRIES TO ARRIVE AT
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AN AGREEMENT ON SETTLEMENT IN GOLD. END SUMMARY.

1. TREASURY REPRESENTATIVES HAD CONVERSATIONS WITH U.K. TREASURY AND BANK OF ENGLAND OFFICIALS WHO ATTENDED LAST WEEK'S C-20 AND WP-3 MEETINGS; U.K. TREASURY SOURCE ALSO ATTENDED JANUARY 21 EC MONETARY COMMITTEE MEETING. THESE OFFICIALS HAVE MIXED VIEWS ON FRENCH DECISION TO FLOAT THE FRANC. U.K. RECEIVED NO ADVANCE WARNING ABOUT THE FLOAT, WHATEVER FRENCH MAY SAY ABOUT EC COORDINATION. THE BANK OF ENGLAND SOURCE SEES FLOAT AS BLATANT COMPETITIVE DEVALUATION, COMPLETELY IN KEEPING WITH FRENCH POLICY DESIGNED TO MAINTAIN AN UNDERVALUED FRANC.

2. AT LEAST PART OF FRENCH RATIONALE FOR FLOATING VIEWED SKEPTICALLY, IN PARTICULAR FRENCH STATEMENTS THAT MOVE TAKEN BECAUSE OF DISAPPOINTING RESULTS OF TALKS ON MONETARY REFORM. U.K. BLAMES THE FRENCH VERY STRONGLY FOR THE DISAPPOINTING RESULTS AND WOULD PARAPHRASE FRENCH STATEMENTS IN TERMS OF "WE DIDN'T COOPERATE IN HELPING TO ACHIEVE REFORM, THEREFORE WE ARE JUSTIFIED IN FLOATING."

3. DURING EC MONETARY COMMITTEE MEETING, JANUARY 21, HABERER OF FRENCH FINANCE MINISTRY ADDED LIGHT RELIEF BY SAYING THAT FRENCH HAD LITTLE EXPERIENCE IN FLOATING AND WOULD BE GRATEFUL FOR ADVICE OF OTHER EC PARTNERS WHICH HAD MORE EXPERIENCE. U.K. TREASURY APPEARS RELAXED ABOUT FRENCH FLOAT, IS APPARENTLY NOT YET WILLING TO CONDEMN IT AS BEGGAR MY NEIGHBOR POLICY. CHANCELLOR BARBER'S COMMENTS IN PARLIAMENT WERE LOW KEY (SEE LONDON 1062). BANK OF FRANCE HAS INTERVENED TO STEADY THE RATE. IN BRUSSELS, FRENCH APPARENTLY ARGUED FLOAT WAS PREFERABLE TO A STEP DEVALUATION, IN WHICH THREE PERCENT DEVALUATION WOULD NOT HAVE BEEN ENOUGH AND 10 PERCENT WOULD BE REGARDED AS TOO MUCH.

4. U.K. TREASURY BELIEVES THAT GISCARD PROBABLY HAS BEEN CONSIDERING THIS MEASURE FOR SOME TIME. IT ALSO BELIEVES THAT POMPIDOU MAY HAVE BEEN FRENCH OFFICIAL MOST RELUCTANT TO AGREE TO IT, IN CONTEXT OF HIS COMMITMENT TO EUROPE. U.K. CONSIDERS THAT POMPIDOU'S HEALTH REMAINS A SERIOUS QUESTION AND THAT GISCARD D'ESTAING IS DOING HIS CONFIDENTIAL

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BEST TO BE IN POSITION TO REPLACE POMPIDOU SHOULD IT COME TO THIS. IN THIS CONTEXT, GISCARD WOULD WANT TO BE SEEN AS DEFENDING FRENCH GROWTH, EXPORTS AND EMPLOYMENT.

5. IN EVENT POMPIDOU WERE TO LEAVE THE SCENE, OUR SOURCES CONSIDER THIS COULD CREATE SOME DIFFICULTIES FOR HEATH, WHO GETS ON WELL WITH POMPIDOU BUT WHO APPARENTLY

DOES NOT HAVE PERSONAL RELATIONSHIP WITH GISCARD.
CHANCELLOR BARBER REPORTEDLY HAS VERY GOOD PERSONAL RELATIONSHIP WITH GISCARD, BUT DID NOT RECEIVE ANY ADVANCE NOTICE OF THE FLOAT. U.K. RIGHTLY OR WRONGLY, BELIEVES

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THAT THERE MAY HAVE BEEN SOME ADVANCE NOTICE GIVEN BY GISCARD TO GERMAN FINANCE MINISTER SCHMIDT IN ROME. U.K. DELEGATION NOTED THAT GISCARD AND SCHMIDT HAD SPENT TIME TOGETHER ON BILATERAL BASIS DURING MEETINGS.

6. U.K. TREASURY PREDICTS HEAVY PRESSURE IN COMING WEEKS WITHIN EC TO ARRIVE AT AGREEMENT TO ALLOW SETTLEMENTS BETWEEN CENTRAL BANKS IN GOLD AT OR NEAR THE MARKET PRICE. IF IT COMES TO THIS, U.K. TREASURY STAFF CONSIDER SOME SLIGHT DISCOUNT ON MARKET PRICE MIGHT BE ALLOWED TO REFLECT DISTURBING ELEMENT IN PRICE IF TRANSACTION HAD TAKEN PLACE THROUGH PRIVATE MARKET RATHER THAN THROUGH MONETARY AUTHORITIES. EC MEETINGS IN EARLY FEBRUARY, INCLUDING BASLE MEETING, AND POSSIBLY AN UNANNOUNCED AND INFORMAL MEETING OF EC FINANCE MINISTERS MAY CONSIDER THE QUESTION. U.K. TREASURY SOURCE SEES U.K. POSITION ON GOLD CHANGING. IT HAS BEEN SALES ONLY UP UNTIL NOW. FRENCH AND ITALIANS, HOWEVER, DO HAVE A REAL PROBLEM GIVEN HIGH PERCENTAGE

OF GOLD IN THEIR RESERVES. U.K. BELIEVES FRENCH MAY PROPOSE ALLOWING MONETARY AUTHORITIES TO PURCHASE GOLD FROM THE FREE MARKET. OSSOLA REPORTEDLY PREPARING A GENERAL PAPER ON GOLD SETTLEMENT FOR EC CONSIDERATION. CONFIDENTIAL

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ONE HALFWAY SOLUTION COULD INVOLVE BORROWING FROM MARKET AGAINST PLEDGING OF GOLD. SOURCE INDICATED THAT SOMETHING HAS TO GIVE SOON ON THIS QUESTION.

7. EC MONETARY COOPERATION VIEWED AS A DISASTER AREA AFTER FRENCH DECISION TO FLOAT. U.K. TREASURY STAFF HOPEFUL THAT THIS MAY BE THE FINAL DEMISE OF THE EC SNAKE. IT IS SKEPTICAL THAT OTHER FLOAT MEMBERS WILL BE ABLE TO ACCOMMODATE THEMSELVES TO THE REMAINING SINGLE STRONG CURRENCY IN THE SNAKE. EVEN IF THEY DO, THERE WILL BE DIFFICULTIES IN WHAT WILL EVENTUALLY EVOLVE INTO A DM BLOC. U.K. HAS NO EXPECTATION NOW OF RECEIVING ANYTHING NEAR WHAT IT CONSIDERS NECESSARY FOR POLITICAL REASONS FROM THE EC REGIONAL DEVELOPMENT FUND, ALTHOUGH GERMAN CHAIRMANSHIP DURING THIS PERIOD COULD OFFER SOME HOPE.

8. U.K. WAS GENERALLY PLEASED WITH OUTCOME OF C-20 MEETING, ESPECIALLY AS AGREEMENT ON SDR VALUATION AND REVISED IMF STRUCTURE HAD BEEN HOPED FOR (SEE LONDON 0390). WITTEVEEN PROPOSAL TO ESTABLISH NEW IMF FACILITY AND HIS COMPETENCE ON THE OTHER TWO ISSUES SEEN AS FIRMLY ESTABLISHING HIM IN THE SADDLE AT THE IMF. THIS MUCH SAID, BANK OF ENGLAND SOURCE NOTED THAT THERE COULD BE DIFFICULTIES IN ESTABLISHING MECHANICS DESIGNED TO IMPLEMENT AREAS OF AGREEMENT. SPECIFICALLY CITED AS PROBLEMS WERE (A) POSSIBILITY THAT SDR VALUATION AS PROPOSED BY WITTEVEEN COULD RESULT IN STRONG SDR BEING CREATED THROUGH THE BACK DOOR, (B) LDC DESIRE TO HOLD OFF ESTABLISHMENT OF NEW IMF COUNCIL UNTIL AGREEMENT REACHED ON INTERNATIONAL MONETARY REFORM, WHICH IS SEEN HERE AS CONTINUED LDC PRESSURE FOR AN SDR/AID LINK; (C) DIFFICULTIES IN ESTABLISHING NEW RECYCLING FACILITY WHICH EVEN UNDER GOOD ASSUMPTION WILL TAKE TIME TO ESTABLISH AND WILL REQUIRE NEW IMF ARTICLES. NONE OF THESE ISSUES WILL BE EASY TO RESOLVE.

9. THERE WAS PRAISE FOR SECRETARY SHULTZ'S PERFORMANCE. U.K. TREASURY SENIOR STAFF APPARENTLY TOOK SECRETARY SHULTZ'S COMMENTS ON BILATERAL DEALS TO HEART

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AND WERE MADE UNCOMFORTABLE BY HIS REMARKS. U.K. TREASURY STAFF REPORT THAT PETER WALKER, HEAD OF DEPARTMENT OF TRADE AND INDUSTRY, HAS BEEN IN THE LEAD IN PRESSING FOR BILATERAL APPROACH. WHEN WALKER WAS IN IRAN IN LATE 1973, HE AND SHAH AGREED TO LINK MONETARY REFORM AND OIL PRICES. U.K. TREASURY WAS TOLD TO WORK OUT THE DETAILS. U.K. TREASURY IS STILL UNCERTAIN WHAT THIS MEANS AND IS ATTEMPTING TO POINT OUT INCONSISTENCIES. OUR CONTACTS REMARKED POINTEDLY THAT CHANCELLOR BARBER (AND DEREK MITCHELL) WOULD BE ACCOMPANYING WALKER ON HIS MEETING JANUARY 25 WITH SHAH OF IRAN IN ST. MORITZ, FOR DISCUSSIONS QUOTE COVERING A RANGE OF ECONOMIC AND FINANCIAL MATTERS UNQUOTE. (LONDON 1053) BRIEFS PREPARED FOR CHANCELLOR BY HIS STAFF REPORTEDLY STRESS THAT C-20 AGREED ON NECESSITY TO AVOID BEGGAR MY NEIGHBOR POLICIES.

10. SOURCES REPORT THAT INCREASED MONEY FLOWS ARE BEING SEEN IN LONDON FROM MIDDLE EASTERN SOURCES, BUT

THEY ARE NOT MASSIVE. FIRMNESS OF EURODOLLAR RATES
INDICATES TO U.K. OFFICIALS THAT THERE ARE STILL MORE
TAKERS THAN LENDERS IN THE MARKET. U.K. CURRENTLY
DEBATING INTERNALLY WHETHER IT WOULD BE CHEAPER TO OBTAIN
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ITS OWN BORROWING THROUGH STERLING OR THROUGH
EUROCURRENCIES WHILE AWAITING, HOPEFULLY BUT WITH SOME
SKEPTICISM, CREATION OF NEW IMF FACILITY.

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